



Testimony of Denise L. Nappier
Treasurer of the State of Connecticut

SUBMITTED TO THE COMMERCE COMMITTEE

MARCH 15, 2011

Senator LeBeau, Representative Berger, and members of the Commerce Committee, thank you for the opportunity to offer testimony concerning **Raised Bill No. 6583, *An Act Concerning Public Employees Benefits Solvency***.

This bill raises a number of policy concerns – not the least of which are the implications for the State having a direct financial interest in the early mortality of its workforce. I will focus my comments, however, on that aspect of the bill that would mandate the purchase of life insurance policies with assets of the State Employees' Retirement Fund.

For the legislature to direct an investment in the manner contemplated by this bill would conflict with the Treasurer's responsibilities as principal fiduciary of the Connecticut Retirement Plans and Trust Funds ("CRPTF"). A transaction of this magnitude and complexity would require comprehensive due diligence before it could be fairly considered.

With that said, based on the limited information provided to my office, it appears that such an investment would not diversify the pension plan's asset/liability risk profile. It is also not clear that an investment in life insurance policies will improve the plan's investment risk and return profile. Whole life insurance policies are illiquid investments. The return from these investments may not provide sufficient compensation for the liquidity risk.

The process by which investment decisions are made bears noting here. Fiduciary duty is the highest standard of duty under the law, and it requires that pension assets, held in trust for beneficiaries, be managed in a way that maximizes income within acceptable levels of risk. Investments for the CRPTF are made within the context of an asset allocation strategy that is specifically crafted for each of the plans and trusts under the CRPTF umbrella. The financial objectives of the CRPTF are long-term in nature and have been established based on a comprehensive review of the capital market assumptions, the demographics of the plan participants, and the anticipated payout of benefits. Only then are investment options considered that will assist in the implementation of these strategic goals.

This methodical approach to investing pension assets is directly responsible for the rebound in the value of the CRPTF. The State's pension funds have posted strong returns for the 2009 and 2010 calendar years, outperforming its benchmarks following the worst recession in generations. The CRPTF returned 12.55 percent for the 2010 calendar year, which represents \$2.8 billion in investment performance. So far this 2011 fiscal year – July 1, 2010 to December 31, 2010 – the pension funds are off to an even stronger start with an investment return of 14.91 percent. This investment performance translates into \$3.2 billion of growth in pension assets. The 2010 calendar year performance represents the second straight calendar year of double digit returns. For calendar year 2009, the pension funds earned 19.8 percent.

This strong recovery is welcome news, particularly given that the funded ratios of the two largest pension plans sponsored by the State – the State Employees' Retirement Fund and the Teachers' Retirement Fund – stand at 44.4 percent and 61.4 percent, respectively. Concerns about the health of our pension funds are warranted, and it is appropriate for this General Assembly to consider strategies that will mitigate the

growth of an unfunded liability that now stands at roughly \$24 billion. Whatever solutions are considered must meet the objective of providing a stream of income to support plan beneficiaries, in order to be financially responsible in the deployment of plan assets. Simply put, we must be able to quantify any proposal and understand the fiscal implications over the long term.

In conclusion, before the merits of any investment are considered, there must first be a threshold determination as to whether such opportunity would fit within the overall asset allocation strategy for the pension plan as a whole; that it properly diversifies, and is beneficial to, the specified asset class; and that it represents the optimum investment opportunity among other choices. Before any investment is placed in the portfolio, it must be part of a competitive search that follows a thoroughly-documented due diligence process. To direct investments in the CRPTF in a manner other than what is planned for in the asset allocation strategy potentially compromises investment performance by reducing the returns otherwise available for a similar level of risk in the capital markets.

For all of these reasons, we must respectfully oppose Proposed Bill No. 6583.